Introduction of Executive Officer System

I. Background

Under the current Commercial Code, board of directors in a Korean company manages and executes the affairs of the company, while simultaneously supervising the status of execution. This may have created inherent limitations of self-monitoring as the board oversees its own activities. As board of directors has primarily focused on the managerial function, there has been much discussion of ways to strengthen the supervisory function of board of directors in order to enhance transparency in corporate governance. Especially, after the Asian financial crisis of the late 1990s, listed companies with assets over KRW 2 trillion must have boards that have at least 50% outside directors. What this means is that most large listed companies in Korea have been managed and run by the representative director and non-registered directors who are, in fact, executive officers. However, Korean laws were silent on executive officers. Accordingly, various issues have been raised in connection with the existence of, and the rights and obligations of, executive officers and their relationship with the board of directors. The recent amendments to the Commercial Code have officially introduced the executive officer system.

II. Appointment of Executive Officers and Relationship with Board of Directors

The amendments allow companies to choose to appoint one or more executive officers with the approval of board of directors and as in the case of directors, the names and resident registration numbers of those executive officers have to be registered with the court. The term of office for executive officers cannot exceed two years unless provided otherwise in the articles of incorporation, but executive officers can be re-elected after expiration of this term. Board of directors, however, can remove an executive officer at any time. As the provisions regarding delegation of authorities in the Civil Act apply mutatis mutandis to the relationship between the company and its executive officers, the relationship is the same as the company's relationship with its directors. The remuneration payable to executive officers is determined by a resolution of the board of directors, unless it is provided for in the articles of incorporation or passed by shareholders meeting.

Executive officers are responsible for the company's management, and make decisions regarding matters delegated by the articles of incorporation or resolution of the board of directors. Once a company appoints an executive officer, it cannot have a representative director, but can have a representative executive officer who plays the same roles as the representative director. If the company has a sole executive officer, then such executive officer will be automatically appointed as the representative executive officer, while the representative executive officer will be elected by resolution of the board of directors if the company has two or more executive officers.

Apart from the executive officers, the board of directors will be composed of directors in accordance with the current legislation and have the authority to monitor the performance of executive officers. In other words, the board of directors will have the authority to appoint/remove executive officers (including representative executive officer), to oversee and audit the status of the execution of duties of executive officers, to delegate decision making power, to allocate duties among executive officers and to determine remuneration to executive officers. The amended Commercial Code does not expressly prohibit directors to concurrently serve as executive officers and some view that it would be possible in practice for directors to serve as executive officers. On the other hand, given that the amended Commercial Code aims to separate the managing body from the supervising body, some view that it would be desirable for directors not to concurrently serve as executive officers. Therefore, it appears that an express legislative provision will be necessary regarding this matter.

III. Duties and Liabilities of Executive Officers

Executive officers owe the same duties as directors: fiduciary duty; duty of loyalty; duty not to compete; duty not to self-deal; duty not to appropriate business opportunities; and duty of confidentiality. Executive officers, in lieu of directors, must report to the board of directors at least once in a quarter. In addition, executive officers have to appear and report to the board of directors whenever so requested. The representative executive officer is also required to report the performance of other executive officers or employees to the board of directors upon request by the board of directors. Moreover, executive officers must accept audits and investigations on their duties by auditor or audit committee. If an executive officer finds any fact that is likely to inflict a substantial loss on the company, he/she must immediately report such to the auditor or audit committee.

An executive officer, like a director, would be liable to the company for damages if he/she acted in violation of any laws or of the articles of incorporation, or neglected to perform his or her duties as an executive officer. Furthermore, an executive officer would be held liable to a third party if he or she neglected to perform his/her duties willfully or by gross negligence causing damages to the third party. In such a case, other executive officers, directors, or auditors who are liable for damages would be jointly and severally liable. As in the case of directors, such liability of executive officers is not only imposed upon the registered executive officers, but it is also imposed on a person who gives an instruction to an executive officer to execute the affairs of the company by exerting his/her influence over the company and a person who is not an executive officer but is deemed to have the authority to execute the affairs of the company by using the job title, such as honorary chairman, chairman, president, managing director or director.

IV. Rationale and Implementation

The rationale behind this amendment of Commercial Code is that, it empowers executive officers to decide and execute management on an exclusive basis, while giving the board of directors the authority to oversee and audit the execution of duties of such executive officers with a view to allowing executive officers to perform their duties in a prompt and efficient manner and the board of directors to fulfill its supervisory functions efficiently. Moreover, the authority to make decisions is delegated to executive officers in order to ensure prompt and efficient decision making. The amendments also provide for appointment of persons who are not directors but have managerial skills as executive officers to increase management efficiency. The executive officer system in the amended Commercial Code is not mandatory provisions. However, considering benefits from the new system, listed companies with de facto non-registered executive officers should consider changing the status of such officers into the executive officers that are newly introduced pursuant to the amended Commercial Code. Before adopting the new system, they need to pay attention to duties and liabilities of executive officers obligated by this amendment of Commercial Code.

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